



AUDITOR-GENERAL
SOUTH AFRICA

The accounting officer
Nkomazi Local Municipality
Private Bag XX 101
Malelane
1320

30 November 2011

Reference: 07464REG10/11

Dear Sir

Report of the Auditor-General on the financial statements and other legal and regulatory requirements of Nkomazi Local Municipality for the year ended 30 June 2011

1. The above-mentioned report of the Auditor-General is submitted herewith in terms of section 21(1) of the Public Audit Act of South Africa read in conjunction with section 188 of the Constitution of the Republic of South Africa section 121(3) of the Municipal Finance Management Act of South Africa (MFMA).
2. In terms of section 121(3) (municipality) of the MFMA you are required to include the audit report in the municipality's annual report to be tabled.
3. Until the annual report is tabled as required by section 127(2) of the MFMA the audit report is not a public document and should therefore be treated as confidential.
4. Prior to printing or copying the annual report which will include the audit report you are required to do the following:
 - Submit the final printer's proof of the annual report to the relevant senior manager of the Auditor-General of South Africa for verification of the audit-related references in the audit report and for confirmation that the financial statements and other information are those documents that have been read and audited. Special care should be taken with the page references in your report, since an incorrect reference could have audit implications.
 - The signature *Auditor-General* in the handwriting of the auditor authorised to sign the audit report at the end of the hard copy of the audit report should be scanned in when preparing to print the report. This signature, as well as the place and date of signing and the Auditor-General of South Africa's logo, should appear at the end of the report, as in the hard copy that is provided to you. The official logo will be made available to you in electronic format.
5. Please notify the undersigned Senior Manager well in advance of the date on which the annual report containing this audit report will be tabled.
6. Your cooperation to ensure that all these requirements are met would be much appreciated.

Kindly acknowledge receipt of this letter.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Phetego Mokgope', written over a dotted line.

Phetego Mokgope
Senior Manager: Mpumalanga

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**REPORT OF THE AUDITOR-GENERAL TO THE MPUMALANGA PROVINCIAL
LEGISLATURE AND THE COUNCIL ON THE NKOMAZI LOCAL MUNICIPALITY
REPORT ON THE FINANCIAL STATEMENTS**

Introduction

1. I have audited the accompanying financial statements of the Nkomazi Local Municipality, which comprise the statement of financial position as at 30 June 2011, and the statement of financial performance, statement of changes in net assets and statement of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information, as set out on pages xxx to xxx.

Accounting officer's responsibility for the financial statements

2. The accounting officer is responsible for the preparation and fair presentation of these financial statements in accordance with South African Standards of Generally Recognised Accounting Practice (SA Standards of GRAP) and the requirements of the Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA), and for such internal control as management determines necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor-General's responsibility

3. As required by section 188 of the Constitution of the Republic of South Africa, 1996 (Act No. 108 of 1996) and section 4 of the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA), my responsibility is to express an opinion on these financial statements based on my audit.
4. I conducted my audit in accordance with International Standards on Auditing and *General Notice 1111 of 2010* issued in *Government Gazette 33872 of 15 December 2010*. Those standards require that I comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.
5. An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.
6. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my audit opinion.

Opinion

7. In my opinion, the financial statements present fairly, in all material respects, the financial position of the Nkomazi Local Municipality as at 30 June 2011, and its financial performance and cash flows for the year then ended in accordance with SA Standards of GRAP and the requirements of the MFMA.

Emphasis of matters

8. I draw attention to the matters below. My opinion is not modified in respect of these matters:

Restatement of corresponding figures

9. As disclosed in note 41 to the financial statements, the corresponding figures for 30 June 2010 were restated as a result of an error noted during the year ended 30 June 2011 in the financial statements of the municipality.

Unauthorised expenditure

10. As disclosed in note 45 to the financial statements, unauthorised expenditure of R89 394 146 was incurred due to an overspending on the total amount appropriated in the municipality's approved budget.

Fruitless and wasteful expenditure

11. As disclosed in note 46 to the financial statements, fruitless and wasteful expenditure of R3 714 281 was incurred due to payments for work not done.

Irregular expenditure

12. As disclosed in note 47 to the financial statements, irregular expenditure of R19 062 401 was incurred due to non-compliance with supply chain management (SCM) requirements.

Material losses

13. As disclosed in note 21 to the financial statements, material losses of R10 935 754 were incurred due to electricity losses.

REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

14. In accordance with the PAA and in terms of *General Notice 1111 of 2010* issued in *Government Gazette 33872 of 15 December 2010*, I include below my findings on the annual performance report as set out on pages xxx to xxx and material non-compliance with laws and regulations applicable to the municipality.

Predetermined objectives

Presentation of information

15. The reported performance against predetermined objectives was deficient in respect of the following criterion:
 - Performance against predetermined objectives was not reported using the National Treasury guidelines.

16. The following audit finding relates to the above criterion:

Reasons for major variances between planned and actual reported targets not provided in report on predetermined objectives

- Adequate explanations for major variances between the planned and the actual reported targets for the objectives were not provided, as required in terms of the relevant reporting guidance. None of the reported targets with major variances were explained.

Usefulness of information

17. The reported performance information was deficient in respect of the following criteria:

- Consistency: The reported objectives, indicators and targets were not consistent with the approved integrated development plan.
- Measurability: Indicators were not well defined and verifiable, and targets were not specific, measurable and time bound.

18. The following audit findings relate to the above criteria:

Reported objectives, indicators and targets not consistent when compared to planned objectives, indicators and targets

- The reported performance against predetermined objectives, indicators and targets was not consistent with the approved integrated development plan.
- The actual achievements with regard to 28% of all planned objectives, indicators and targets specified in the integrated development plan for the year under review were not included in the report on predetermined objectives submitted for audit purposes.

Changes to planned objectives, indicators and targets not approved

- Different objectives, indicators and targets were reported on, compared to those approved in the integrated development plan. These different objectives, indicators and targets were not included in the approved or adjusted budgets.

Changes to planned objectives, indicators and targets not disclosed in report on predetermined objectives

- Changes to the objectives, measures and targets in the approved annual performance plan were not disclosed and explained, as required in terms of the relevant National Treasury preparation guide.

Planned and reported targets not specific, measurable and time bound

- For the selected objectives, 32% of the planned and reported targets were not:
 - specific in clearly identifying the nature and the required level of performance
 - measurable in identifying the required performance
 - time bound in specifying the time period or deadline for delivery.

Reliability of information

19. The reported performance information was deficient in respect of the following criteria:

- Validity: The reported performance did not occur and does not pertain to the entity.

- Accuracy: The amounts, numbers and other data relating to reported actual performance were not recorded and reported appropriately.
- Completeness: All actual results and events that should have been recorded had not been included in the reported performance information.

20. The following audit finding relates to the above criteria:

The corroborating evidence did not agree with the reported explanations for major variances between planned and actual reported targets

- Corroborating evidence provided as a basis for the explanations for major variances between the planned and the actual reported targets did not agree in all instances with the reasons for the variances reported.

Compliance with laws and regulations

Annual financial statements

21. The financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122 of the MFMA. Material misstatements in capital assets, current assets, liabilities, revenue, expenditure and disclosure items identified by the auditors were subsequently corrected, resulting in the financial statements receiving an unqualified audit opinion.

Expenditure management

22. The municipality did not recover unauthorised, irregular as well as fruitless and wasteful expenditure from the liable person, as required by section 32(2) of the MFMA.
23. The accounting officer did not take reasonable steps to prevent unauthorised, irregular as well as fruitless and wasteful expenditure, as required by section 62(1)(d) of the MFMA.

Procurement and contract management

24. Goods and services with a transaction value between R10 000 and R200 000 were procured without obtaining written price quotations from at least three different prospective providers, as per the requirements of SCM Regulation 17(a) and (c).
25. Quotations were accepted from prospective providers who were not on the list of accredited prospective providers and who did not meet the listing requirements prescribed by the SCM policy, in contravention of SCM Regulations 16(b) and 17(b).
26. Awards were made to suppliers who did not submit a declaration on their employment by the state or their relationship to a person employed by the state, as per the requirements of SCM Regulation 13(c).
27. The preference point system was not applied in all procurement of goods and services above R30 000, as required by section 2(a) of the Preferential Procurement Policy Framework Act of South Africa, 2000 (Act No. 5 of 2000) (PPPFA) and SCM Regulation 28(1)(a).

28. Awards were made to suppliers based on preference points that had not been calculated in accordance with the requirements of the PPPFA and its regulations.
29. The municipality did not implement an SCM policy, as required by section 111 of the MFMA.
30. Awards were made to providers who were persons in the service of the municipality or whose directors and principal shareholders were persons in the service of the municipality, in contravention of SCM Regulation 44. Furthermore, the providers failed to declare that they were in the service of the municipality, as required by SCM Regulation 13(c).
31. Awards were made to providers who were persons in the service of other state institutions or whose directors and principal shareholders were persons in the service of other state institutions, in contravention of the requirements of SCM Regulation 44.
32. Persons in the service of the municipality who had a private or business interest in contracts awarded by the municipality failed to disclose such interest, as required by SCM Regulation 46(2)(e) and the code of conduct for staff members issued in terms of the Municipal Systems Act of South Africa, 2000 (Act No. 32 of 2000) (MSA).
33. Persons in the service of the municipality whose close family members had a private or business interest in contracts awarded by the municipality failed to disclose such interest, as required by SCM Regulation 46(2)(e) and the code of conduct for staff members issued in terms of the MSA. The providers also failed to declare their relationship to persons employed by the municipality as per the requirements of SCM Regulation 13(c).
34. SCM officials whose close family members had a private or business interest in contracts awarded by the municipality participated in the process relating to that contract, contrary to the requirements of SCM Regulation 46(2)(f).

Transfers and conditional grants

35. The allocation of the municipal infrastructure grant was utilised for purposes other than those stipulated in the respective schedules or gazetted in the Division of Revenue Act of South Africa, 2010 (Act No. 1 of 2010) (DoRA) framework, in contravention of the requirements of section 15(1) of DoRA.

Budget

36. Unforeseeable and unavoidable expenditure not provided for in the annual budget was incurred but was then not appropriated in an adjustment budget, as required by section 29(2)(d) of the MFMA.

INTERNAL CONTROL

37. In accordance with the PAA and in terms of *General Notice 1111 of 2010* issued in *Government Gazette 33872 of 15 December 2010*, I considered internal control relevant to my audit, but not for the purpose of expressing an opinion on the effectiveness of internal control. The matters reported below are limited to the significant deficiencies that resulted in the findings on the annual performance report and the findings on compliance with laws and regulations included in this report.

Leadership

- 38. The accounting officer did not exercise oversight responsibility over financial and performance reporting, compliance with laws and regulations as well as internal control.
- 39. Actions were not taken to address risks relating to the achievement of complete and accurate financial and performance reporting.
- 40. The systems were not documented in the policy and procedures manual, while the results of the monitoring process were not routinely communicated to all managers and staff.

Financial and performance management

- 41. Pertinent information was not identified and captured in a form and time frame to support financial and performance reporting.
- 42. Requested information was not available and supplied without any significant delay.
- 43. The municipality did not have competent individuals who understood the financial reporting framework and performance management requirements.
- 44. Manual or automated controls were not designed to ensure that the transactions had occurred, were authorised, and were completely and accurately processed.

Governance

- 45. Ongoing monitoring and supervision were not undertaken to enable an assessment of the effectiveness of internal control over financial and performance reporting.

Auditor-General

Nelspruit

30 November 2011



AUDITOR-GENERAL
SOUTH AFRICA

Auditing to build public confidence